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TODAY

THE CHAIRMAN of the Sovran Financial Corp. said the long-term strength of the company was his top concern, in response to critics of the $654 million purchase of Commerce Union. While noting that the price was not excessive, industry analysts calculated that the move would mean dilution of about 8% for Sovran's owners.....3

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There are serious long-term problems in Latin America. Brazil is in the limelight now, but who will be next?

William King, vice president and research director for McCarthy, Crisanti & Maffei Inc., on the impact of Latin debt on U.S. banks [Page 1]

Unquote

Discover Card Could Make Sears Largest Issuer

By LISABETH WEINER
Midwest Bureau

CHICAGO — Sears, Roebuck and Co. is close to surpassing Citicorp to become the nation's largest issuer of revolving bank credit cards.

Sears disclosed this week that its Dean Witter Financial Services Group has 15 million Discover cards in circulation, up from 11.5 million at yearend 1986.

Credit Cards

Only 15 months after its national launch, Discover is closing in on Citicorp's industry-leading bank card total, which experts estimate at between 15 million and 16 million MasterCard and Visa cards combined.

Discover cards are not often compared with bank cards because they are

Sears: Page 15 ➤

Merrill Ta... In Mortgage Securities Trading

By JED HOROWITZ

NEW YORK — Merrill Lynch & Co. announced Wednesday it has lost $250 million from trading mortgage-backed securities and said it has fired a senior trader held partly responsible.

The company is the first victim of the recent jump in interest rates that has sparked rumors of trading losses throughout Wall Street.

However, Merrill blamed the loss in part on "significant unauthorized activity" by Howard A. Rubin, a vice president and mortgage-backed securities trader, as well as on market volatility.

A Merrill spokesman would not comment on how much of the loss was due to any unauthorized trading. Mr. Rubin could not be reached for comment.

Analysts who attended a meeting at Merrill on Wednesday said the pretax loss occurred on $1 billion of Government National Mortgage Association securities that Merrill marked down to $750 million.

Merrill had purchased $500 million of the Ginnie Mae securities and converted them into strips. In a strip, a firm separates the interest portion of a security from the principal, auctioning each off separately. Merrill sold the interest portion quickly, but was stuck with the principal-only portion because of low liquidity and rising interest rates, analysts said.

The remaining $500 million of the position was purchased without authorization by Mr. Rubin, according to analysts who were briefed by Jerome P. Kenney, head of Merrill's capital markets division.

Sources in the mortgage-trading department said Mr. Rubin was suspended Monday and fired Wednesday.

Mr. Rubin's responsibilities in mortgage-backed trading had been broadened earlier this year to include trading collateralized mortgage obligations and government agency securities. Mr. Rubin was the sole employee to be dismissed over the loss, according to

Merrill: Page 15 ➤

Brazil Toll at 25 Banks: $15.6 Billion of Loans Reclassified

By LISABETH WEINER
Midwest Bureau

CHICAGO — Twenty-five of the largest U.S. bank holding companies put more than $15.6 billion worth of medium- and long-term loans to Brazil on nonaccrual status during the first quarter, according to an *American Banker* survey.

This means that interest on the debt will be recorded only at the time payment is actually received.

The loans these banks put on nonaccrual represent about 70% of the banks' total loans to that country.

During the first quarter, the same banks also put nearly $1.4 billion of Ecuadoran loans on a cash basis, according to the survey. The decision to put the Ecuadoran loans on nonaccrual status followed news of an earthquake that ravaged oil pipelines in that Latin American country. Oil is a major source of Ecuador's revenues.

As a result of these two actions, first-quarter earnings for these banks were reduced by $253 million, according to the

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survey. Full-year earnings for all the banks could be clipped by about $912 million unless Brazil negotiates a new credit agreement with its more than 700 creditor banks by yearend.

After U.S. regulators reclassified the Brazilian debt as substandard, most banks, though not all, put their medium- and long-term debt to that country on a nonaccrual, or cash, basis.

For many banks this action increased the level of first-quarter nonperforming loans, and in some cases resulted in lower first-quarter earnings.

For the largest U.S. bank creditors to Brazil, these non-

Brazil Toll: Page 2 ➤

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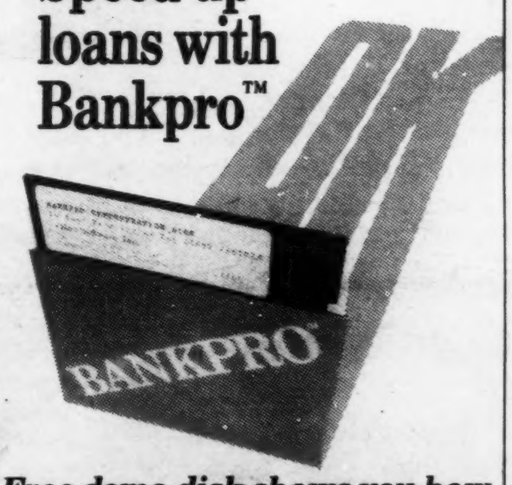

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Brazil Toll: $15.6 Billion of Bank Loans Reclassified

➡ Continued from Page 1

performing loans also represent a sizable percentage of shareholders' equity. For Citicorp, the $3.8 billion of Brazilian debt placed on nonaccrual is about 40% of shareholders' equity. At Chase Manhattan Corp., $2.3 billion of nonperforming Brazilian debt is slightly more than 50% of $4.3 billion in shareholders' equity recorded at the end of the first quarter.

Meanwhile, bankers have expressed high levels of frustration with Brazil's unilateral decision on Feb. 20 not to remit interest payments on its foreign debt, an action described as severe and extreme. What may differentiate these negotiations from other Latin American credit restructurings of the past is that the bankers are likely to demand that a realistic and flexible plan be devised.

'A Pemanent-Temporary Solution'

"We see the Brazil debt being resolved this year. But it will be a permanent-temporary solution," said William King, vice president and research director for McCarthy, Crisanti & Maffei Inc. "There are serious long-term problems in Latin America. Brazil is in the limelight now, but who will be next?"

Mr. King is confident that the Brazilian debt situation will be resolved in 1987 and that the loans will, at least to some degree, return to a performing basis. "The debt is so large and there is so much political pressure that we just expect that somehow it will be worked out," he added.

Perhaps the most encouraging news supporting that position may be the resignation earlier this week of Brazilian Finance Minister Dilson Funaro, who instituted the debt moratorium. His replacement, economist Luiz Carlos Bresser Pereira, is likely to seek a compromise in foreign debt negotiations.

And the banking community seems optimistic that a renegotiated settlement will be reached before year's end.

At a press conference earlier this month, First Chicago Corp. chairman Barry Sullivan said it is probable that the debt renegotiations will be accomplished in 1987. "I don't think it's a sure thing, but I think it's probable."

Brazil Resists Scrutiny

Mr. Sullivan, who met with the former Brazilian finance minister in early April, sees two issues confronting Brazil. The first is Brazil's unwillingness to subject itself to external scrutiny and a program of monitoring. While this has been "very central" to debt negotiations with other countries, Brazil is resisting it, he said. The second issue is finding new, flexible instruments for the banks that will give the creditors more options in dealing with the restructured debt.

"I don't doubt the will of Brazil, which is to refinance," Mr. Sullivan said. "Brazil needs, in that refinancing, some new money, and they need the new money because they want to keep the plant and equipment up to date. They have a heck of an incentive to renegotiate, but they want to do it on a basis that they [can] live with longer-term," Mr. Sullivan said.

Meanwhile, U.S. bank regulators would like to be optimistic that an agreement with Brazil will be negotiated this year. But one source said a more likely scenario is that U.S. creditors may receive a kind of good-faith payment from Brazil. "My guess is," he said, "that in the second half of 1987 the banks will receive interest payments from Brazil. . . . It will not be enough to take the loans off nonaccrual status, but it will be enough to recapture some interest income."

Neal Farrell, vice chairman of Mercantile Bancorp., said the one thing differentiating the Brazilian debt situation from that of other Latin American countries is that Brazil is not destitute and does have the money to meet its interest obligations; it has just chosen not to remit payment. "The money owed is being kept in Brazil. This difference is a fine line, but it's an important line," Mr. Farrell said.

Unhappy Bankers

What is clear at this point, Mr. Farrell said, is that "all of the U.S. banks have been materially hurt by lower earnings, and the impact is hitting home to Brazil that there are unhappy bankers and unhappy shareholders out there." St. Louis-based Mercantile put $66.1 million of Brazilian loans and $3.1 million of Ecuadoran loans on nonaccrual status, which reduced first-quarter earnings by $798,000.

The extent of this unhappiness is being made known by a growing number of regional bankers who want to reduce their Latin American debt exposure. They are not eager to throw good money after bad — that is, to cough up additional new loans that might be mandatory under a restructuring but that might not resolve the country's long-term economic plight. Even Citibank has started to balk at granting concessions to some debtor countries.

In the past, Mr. Farrell said, debt restructurings have been negotiated by a steering committee made up of money center banks that simply told the smaller banks how much would be required in new money loans. A lot of people felt then that they were just throwing good money after bad, he said. "Then we found two years later we were doing it again, like a treadmill. It became the ultimate treadmill," he added.

Regionals Speak Out

The money center lenders to Latin American have made very little effort to get the smaller banks to participate in the restructuring talks in the past, Mr. Farrell said. "Regional bankers don't have time and we don't have a staff of officers who can get involved in a steering committee, so it's probably impractical on a day-to-day basis."

But the regional banks are getting more vocal in letting the Latin American countries and the money center banks know where they stand with regard to restructured debt.

"We're not clamoring to leave Brazil or Mexico totally," Mr. Farrell said. "We have done business there for 75 years and it was good, strong business for many years. But we have to find a way of working with them. The pressure is on to find a sensible way of dealing with the situation."

Smaller banks are intrigued with a number of new techniques that have been mentioned as a way for them to reduce their exposure to Brazil in a renegotiated debt accord. For instance, while it may not be the most lucrative option, there is a thinly traded market for the sale of Latin American credits. Currently that market is paying about $0.62 for each dollar of Brazilian debt and $0.55 for each dollar of debt to Mexico.

Debt-for-Equity Swaps

Another alternative some banks have explored is a debt-for-equity swap, which essentially allows a creditor to trade a certain amount of debt for an equity position in a Brazilian company.

Michael Moore, who heads Latin American business for Norwest Corp., Minneapolis, said earlier this month that his bank traded $12.5 million of Brazilian debt for a 14% interest in a Brazilian paper company. Mr. Moore termed it a "great deal" because it allows Norwest to continue doing business in Brazil while reducing its exposure. And that supports his contention that despite the current round of problems, there is an underlying economic strength in Brazil.

A recently negotiated debt restructuring with Argentina has in fact implemented such innovations as debt-for-equity swaps, and may become a model for future Latin American debt restructurings. "This Argentina negotiation," one regulator said, "may be the threshold for negotiating a menu of alternatives that satisfies the portfolio preference of very small regional or [superregional] banks."

One major point of contention has been using a bank's 1982 loan exposure level as the base for determining the amount of money to be put into a new credit agreement. In the Argentina accord the base date will be adjusted to account for debt that has been forgiven or debt that has been swapped into equity.

"It's more realistic to use a current base rather than a 1982 base," said Mr. Farrell of Mercantile. "Nobody feels good about putting up additional money based on losses that have already been sustained by your organization."

Using this menu approach for debt negotiations has been widely proposed by people like William Cline, an international debt expert from the Institute for International Research. "What you want to do here is tailor the vehicle to meet the interest of the particular bank."

A United Front

Meanwhile, negotiating the Brazilian and future Latin American debt will get more difficult, especially as each country hopes to improve upon the terms given to one of the other countries. "Banks have to stick together," said Mr. King of McCarthy, Crisanti & Maffei. "Banks have to try as best they can not to give in to each new demand that is more favorable than the previous demand, or it will just be a continuous cycle. Banks have simply got to stand together and say no, we're not going to provide any more favorable terms than you've got now."

While some of that "stick-togetherness" may be waning as regional banks and even Citibank have expressed an unwillingness to just hand out new money on restructured loans, the effect of this has been offset by the inability of the Latin American countries to form a debtors' cartel. "There are some very nationalistic feelings in the Latin American countries," Mr. King said. "Each country thinks maybe he's better than the guy next door and should get better terms."

While some bankers have expressed concern that other Latin American countries may attempt to mimic Brazil's action, Mr. Farrell does not expect that to happen. "Other Latin countries have disassociated themselves from Brazil's course of action. It was severe and extreme, and Brazil alienated itself," he said. "Brazil played the ultimate trump card. But the next move belongs to the banks." ■

Reclassified Brazil and Ecuador Loans Take Toll on Bank Holding Company Earnings

March 31 Data (In Millions of Dollars)

	Brazil Nonaccrual	Ecuador Nonaccrual	1st Qtr Impact	Full Year Impact
Citicorp, New York[1]	$3,800	$324	$56.0	$202.0
Chase Manhattan, New York[1]	2,300	280	36.6	146.4
BankAmerica Corp., San Francisco	1,900	180	47.0	150.0
Manufacturers Hanover Corp., New York[2]	1,400	150	21.0	72.0
J.P. Morgan & Co. Inc., New York[2]	1,300		20.0	72.0
Chemical New York Corp., New York	1,041	52	12.0	51.0
Bankers Trust New York Corp., New York	540	42	7.9	30.0
Wells Fargo & Co., San Francisco	423	29	7.0	24.0
Security Pacific Corp., Los Angeles	401	73	7.2	26.0
First Chicago Corp., Chicago	386	34	5.2	20.8
Continental Illinois Corp., Chicago	376	25	10.9	37.0
Marine Midland Banks, Inc., Buffalo[4]				
First Interstate Bancorp., Los Angeles	320	14	4.6	15.4
Mellon Bank Corp., Pittsburgh[5]	307	27		
Bank of Boston Corp., Boston	183	33	3.0	9.0
Irving Bank Corp., New York	215	33	4.4	15.3
Republic New York Corp., New York	179	0	2.4	9.8
Norwest Corp., Minneapolis	165	16	1.9	7.7
First Bank System, Inc. Minneapolis	140	9	1.7	6.9
PNC Financial Corp. Pittsburgh[1]	98	19	1.4	5.6
NCNB Corp., Charlotte, N.C.	77	14	1.4	5.6
Bank of New England Corp., Boston[1]	59	6	0.8	3.2
MCorp, Dallas	23	8	0.7	2.5
SunTrust Banks, Inc., Atlanta	20	22	N.A.	N.A.
NBD Bancorp., Inc., Detroit[6]	7	4	N.A.	N.A.
TOTALS	$15,660	$1,394	$253.1	$912.2

Source: Company earnings reports. [1] Full year impact is estimate by American Banker. [2] Projection of full-year impact covers Brazil only. [3] Ecuador exposure not disclosed. [4] Loans not placed on nonaccrual status until payment of principal or interest is 90 days past due. At March 31, Marine's total loans to borrowers in Brazil were $620.9 million, of which $4.3 million were on nonaccrual status. About $348.4 million of Marine's Brazilian loans are medium- or long-term. Because of uncertainty over the Brazilian loans, Marine has established a special reserve against interest due on the medium- and long-term loans. This resulted in a pretax provision of $9.7 million, which reduced first-quarter earnings by $6.7 million. [5] After-tax figures not available. Pretax impact of Brazilian loans was $9 million in the first quarter. Impact for the year is estimated at $25 million. The effect from Ecuador is insignificant. [6] Effect on earnings negligible.

Corrections

An article on April 29 ("Branch Banking Sweeps Texas in Challenge to State Officials," page 1) incorrectly reported the number of banks in Texas. The correct number is 1,900.

□

An article on April 28 ("Merrill Offers Two Issues of Japanese Bank Deposit Notes," page 16) incorrectly identified one of the issuing banks. The institution involved is Sumitomo Trust & Banking Co. Ltd., New York, not Sumitomo Ltd. ■